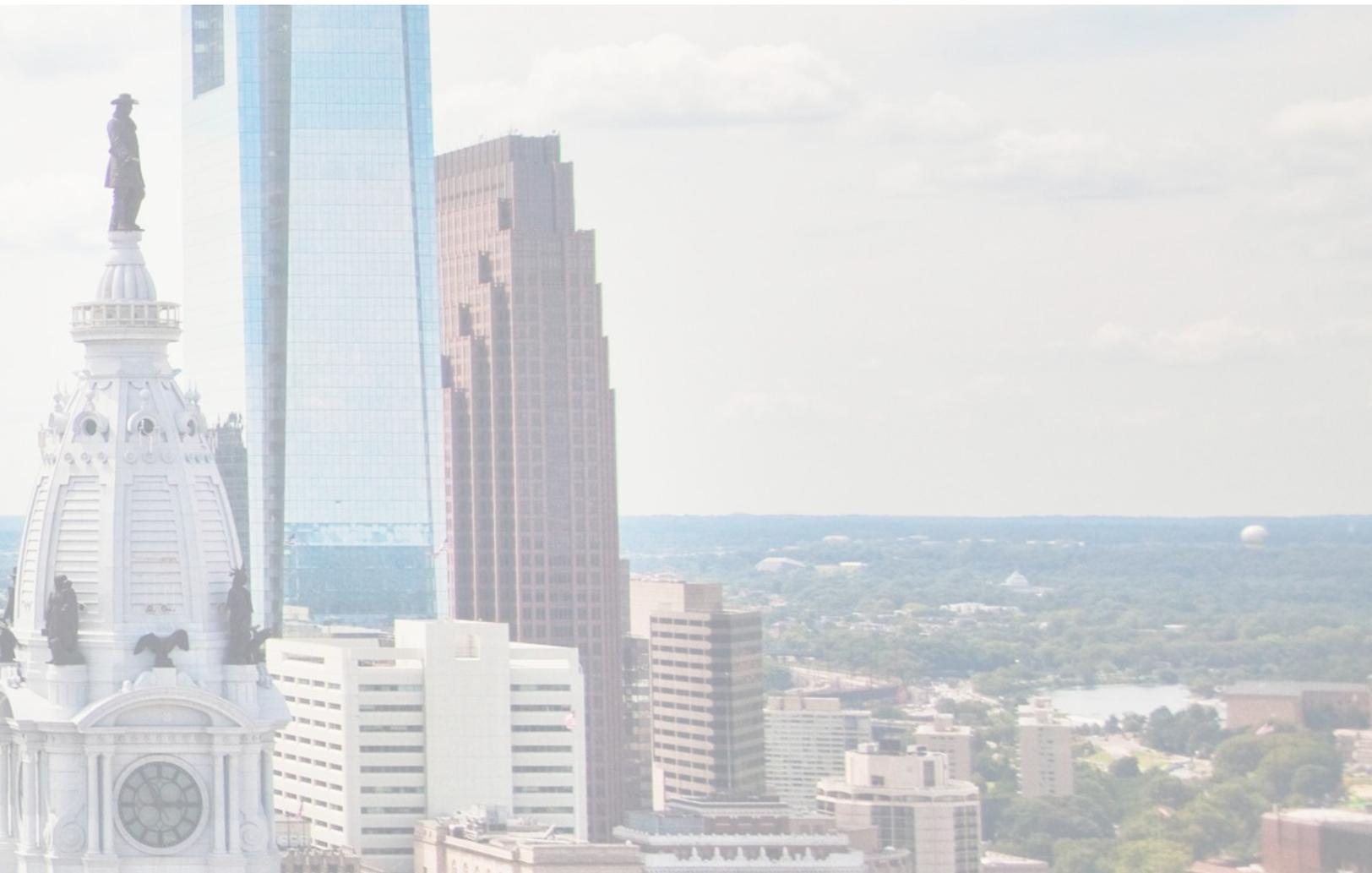


Report on Internal Control and On Compliance and Other Matters School District of Philadelphia Fiscal Year 2022



City of Philadelphia, Pennsylvania
Office of the Controller
Charles Edacheril
Acting City Controller



CITY OF PHILADELPHIA

OFFICE OF THE CONTROLLER
1230 Municipal Services Building
1401 John F. Kennedy Boulevard
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CHARLES EDACHERIL
Acting City Controller

April 12, 2023

Reginald L. Streater, Esq., Board President
Board of Education
440 N. Broad Street, Suite 101
Philadelphia, PA 19130

Dear Mr. Streater,

In accordance with the Philadelphia Home Rule Charter, the Office of the Controller conducted an audit of the basic financial statements of the School District of Philadelphia, Pennsylvania ("School District") as of and for the fiscal year ended June 30, 2022, and has issued its Independent Auditor's Report dated February 14, 2023.

In planning and performing our audit, we considered the School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing an opinion on the effectiveness of the School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the School District's internal control over financial reporting.

Attached is our report on Internal Control over Financial Reporting and on Compliance and other matters dated February 14th, 2023. The findings and recommendations contained in the report were discussed with management. We have included management's written response to the findings and recommendation as part of the report. We believe that if implemented by management, the recommendations will improve the School District's internal control over financial reporting.

We would like to express our thanks to the management and staff of the School District for their courtesy and cooperation in the conduct of our audit.

Respectfully submitted,

Charles Edacheril

Charles Edacheril, CPA
Acting City Controller

CC: Board of Education Members
Tony Watlington., Ed.D., Chief Executive Officer and Superintendent of Schools
Mayor James F. Kenney
Michael Herbstman, Chief Financial Officer
Marcy F. Blender, CPA, Deputy Chief Financial Officer and Comptroller



SCHOOL DISTRICT OF PHILADELPHIA FISCAL YEAR 2022 REPORT ON INTERNAL CONTROL AND ON COMPLIANCE AND OTHER MATTERS

EXECUTIVE SUMMARY

Why the Controller's Office Conducted the Audit

In accordance with the Philadelphia Home Rule Charter, the Office of the City Controller audited the School District of Philadelphia's (School District) basic financial statements as of and for the fiscal year ended June 30, 2022 for the purpose of opining on its fair presentation. As part of this audit, we reviewed the School District's internal control over financial reporting to help us plan and perform the examination. We also examined compliance with certain provisions of laws, regulations, contracts, and grant agreements to identify any noncompliance that could have a direct and material effect on financial statement amounts.

What the Controller's Office Found

The Controller's Office found that the School District's financial statements were presented fairly, in all material respects in accordance with accounting principles generally accepted in the United States of America and issued a separate report that accompanies the School District's Annual Comprehensive Financial Report (ACFR) for the fiscal year ended June 30, 2022. The audit procedures used to arrive at our conclusion regarding these financial statements led us to identify matters involving the School District's internal control over financial reporting that require management's attention. Some of the more important matters include:

- Inadequate review of access controls and segregation of duties continue to remain within the School District's Oracle system including the identification of incompatible roles, responsibilities and permissions, which may potentially allow a system user with access commensurate with their job duties.
- Outstanding termination pay due to former employees in the amount of \$1.4 million due to almost 200 employees. The School District would appear to be in violation of applicable labor agreements by not distributing the funds in a timely manner.

What the Controller's Office Recommends

The Controller's Office has developed a number of recommendations to address the findings noted above. These recommendations can be found in the body of the report.

**AUDITOR'S REPORT ON INTERNAL
CONTROL AND ON COMPLIANCE
AND OTHER MATTERS**

**SCHOOL DISTRICT OF
PHILADELPHIA**

FISCAL 2022



CITY OF PHILADELPHIA

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CHARLES EDACHERIL
Acting City Controller

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the President and Members of
The Board of Education of the
School District of Philadelphia

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States (*Government Auditing Standards*), the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the School District of Philadelphia, Pennsylvania (School District), a component unit of the City of Philadelphia, Pennsylvania, as of and for the year ended June 30, 2022, and the related notes to the financial statements, which collectively comprise the School District's basic financial statements, and have issued our report thereon dated February 14, 2023.

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the School District's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School District's internal control. Accordingly, we do not express an opinion on the effectiveness of the School District's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

CITY OF PHILADELPHIA
OFFICE OF THE CONTROLLER

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control described in the accompanying report as item 2022-001 that we consider to be a significant deficiency.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the School District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Other Conditions

We noted certain conditions that are not required to be reported under *Government Auditing Standards*, but nonetheless represent deficiencies in internal control that should be addressed by management. These other conditions are listed in the table of contents and described in the accompanying report as item 2022-002 to 2022-005.

School District's Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the School District's response to the findings identified in our audit and described in the accompanying report. The School District's response was not subjected to the other auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



CHARLES EDACHERIL, CPA
Acting City Controller
Philadelphia, Pennsylvania
February 14, 2023

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SIGNIFICANT DEFICIENCIES

2022-001 INADEQUATE REVIEW OF ACCESS CONTROLS AND SEGREGATION OF DUTIES

Condition: Prior year testing noted that a formally documented Segregation of Duties (SoD) policy, including identification of incompatible roles, responsibilities, and permissions, has not been established. Users have been assigned access based upon job function role and location, however the specific access permissions of the roles have not been reviewed by the School District of Philadelphia (School District). Due to this condition, identification of incompatible permissions within roles or across roles has not been performed. In addition, a periodic user access review has not been performed since the implementation of the system which went live July 1, 2020. Finally, a documented security program or policy, which includes the School District's responsibilities over the Oracle system, was not provided. Our current year follow up disclosed that as of June 30, 2022, corrective action to prevent the recurrence of this condition has not been implemented.

Criteria: Although the Oracle system is a vendor hosted system, there are aspects of the security and provisioning of access to the system, which is the responsibility of the School District. Incompatible roles, responsibilities, and permissions should be established to enforce SoD in both the provisioning and the periodic reviewing of user access.

Effect: There may be users with access not commensurate with their job responsibilities. In addition, users may have access across incompatible roles, responsibilities and permissions within the system, thereby potentially allowing a user to bypass system controls.

Cause: As part of the implementation of the system, there was not a required step to identify incompatible user access permissions. A periodic review of access has not been performed due to the current focus on the implementation of the Oracle HR system.

Recommendation: The School District should formally identify the areas of responsibility related to security and provisioning of access related to the Oracle system and include them in an overall security program or policy. As part of this security program or policy, a requirement for the performance of a periodic access review should be included. There should also be a comprehensive document that clearly identifies incompatible roles, responsibilities, and permissions. These SoD considerations should be included in the periodic access reviews [306021.01].

OTHER CONDITIONS

2022-002 TERMINATION PAYMENTS REMAIN OUTSTANDING

Condition: In our prior year report we commented that the School District owed \$2.7 million to over 500 former employees that separated from service as far back as 2019. As of June 30, 2022, the School District processed 352 cases of the backlogged termination payment cases from 2020 and prior.

At the conclusion of our fiscal 2022 audit, we found that termination payments totaling \$1.4 million due to almost 200 former employees that separated from service, still have not been distributed. Table 1 below summarizes the amount of termination pay applicable to the two groups of former employees – those that are age 55 and older, which receive their compensation via a contribution to a tax-sheltered annuity plan; and those under the age of 55 that are compensated by check.

Table 1: Employee termination pay outstanding for more than one year as of June 30, 2022

Column A	Column B	Column C	Column D	Column E
Fiscal year of separation	Number of employees owed termination pay	Termination pay owed to those age 55 & over at separation (in thousands)	Termination pay owed to those under age 55 at separation (in thousands)	Total termination pay owed (in thousands) (Col. C+D)
2021	149	\$1,240	\$36	\$1,276
2020	28	\$74	\$64	\$138
2019	13	\$17	\$2	\$19
2016	1	\$2	\$0	\$2
Total	<u>191</u>	<u>\$1,333</u>	<u>\$102</u>	<u>\$1,435</u>

Source: Prepared by the Office of the Controller based on the analysis of the School District’s Vacation, Personnel, and Illness Leave Report (VPIL).

Criteria: Under the current labor agreements with many of its unionized employees, when an employee separates from School District employment, they are entitled to termination pay for the unused time within 30-75 days of their separation¹.

Effect: The School District would appear to be in violation of applicable labor agreements.

Cause: In previous years, School District management had difficulty dedicating the necessary resources to address outstanding termination pay owed to employees that have separated from the School District.

Recommendation: Management for the School District should prioritize processing any outstanding termination payments owed to separated employees to ensure that the School District is in compliance with current labor agreements. [600121.01]

¹ The length of time for each of the contracts is as follows: 32BJ 1201 Building Engineers / Craftsmen – 30 days; School Police Association of Philadelphia – 60 days; Philadelphia Federation of Teachers – 75 days; and the Commonwealth Association of School Administration – 75 days. The number of days applicable to food service is not specified in their labor agreement with the School District.

2022-003 INADEQUATE DEPROVISIONING OF SYSTEM ACCESS

Condition: Prior year testing noted that for one (1) out of 25 terminated users tested, the user's system access was not disabled in a timely manner. The user was suspended without pay, awaiting a board decision for termination, however, the user's access was not disabled during the period between suspension and approval of termination. Our current year follow up disclosed that as of June 30, 2022, corrective action to prevent the recurrence of this condition had not been implemented.

Criteria: When a user is suspended or terminated, their system access should be disabled in a timely manner.

Effect: Unauthorized system access is maintained, allowing a user to perform unauthorized transactions.

Cause: Human Resources received notification from the Labor Relations team after the board approved the termination. At which time, the user's access was disabled. The date of suspension awaiting approval of termination was not provided to trigger the disabling of access.

Recommendation: When a user is suspended awaiting termination, notification should be provided to Human Resources who can update the system in a timely manner to trigger the user's access to be disabled [306021.02].

2022-004 NO FORMAL POLICY FOR CONFIGURATION CHANGES

Condition: Prior year testing noted that a formal policy for configuration changes, including the procedures for requesting changes from Oracle and the supporting vendor, is not maintained. In addition, a formal list of change requests, including Oracle requested changes, configuration changes, and emergency changes, is not maintained. Our current year follow up disclosed that as of June 30, 2022, a formal policy for configuration changes had not been implemented.

Criteria: A formal configuration change management policy should be maintained that captures the various types of changes that can be made to the system and required steps in the identification, testing, approval, and implementation of changes. As defined by the policy, a formal list of change requests should be maintained.

Effect: Without a documented configuration change management process, there is a risk of unauthorized changes, and changes that have not been tested before implementation. This could affect the operations of the system.

Cause: During the Oracle system implementation, the supporting vendor was responsible for defining and enforcing the change management process. When the system was implemented, the School District established a change management process, however it was not formally documented.

Recommendation: A formal policy for configuration changes should be maintained that captures the various types of changes that can be made to the system. The policy should include the required steps in the identification, testing, approval, and implementation of changes. As defined by the policy, a formal list of change requests should be maintained, such as with a ticketing system, or be maintained by those who are not responsible for initiating, performing, testing, or approving changes [306021.03].

2022-005 INADEQUATE MONITORING OF THIRD-PARTY SYSTEM CONTROL REPORTS

Condition: Prior year testing noted that there is no formal, documented review of the Oracle Fusion Service Organization Control (SOC) 1 report. Our current year follow up disclosed that as of June 30, 2022, a process for the formal documented review of SOC reports had not been implemented.

Criteria: Reliance on a third party to support key processes require formalized monitoring controls by the School District to ensure that any issues at the third party are evaluated for impact to the School District. In addition, hand-off controls between the third party and the School District should be identified and formalized. SOC reports are AICPA defined reports which are performed by public accounting firms to evaluate and report on the controls at a third-party service provider. SOC reports allow management and auditors to gain comfort over controls at a third-party service provider without the need to perform their own audit procedures.

Effect: Formal review of SOC reports is not documented. In addition, there is an increased risk of unauthorized access.

Cause: The Oracle Fusion SOC 1 report was not originally made available by the vendor.

Recommendation: An annual review of the Oracle Fusion, and other applicable SOC reports should be formally documented. This includes evaluating any exceptions in the report, mapping of Complementary User Entity Controls (CUECs) to controls within the School District, and review of any subservice organization's SOC report [306021.04].

RESPONSE TO AUDITOR'S REPORT



Michael Herbstman
Chief Financial Officer

Office of The Chief Financial Officer
440 North Broad Street, Suite 304
Philadelphia, PA 19130
(215) 400-4500
Fax (215) 400-4501

March 24, 2023

Mr. Charles Edacheril, CPA
City of Philadelphia
Office of the Controller
1230 Municipal Services Building
1401 John F. Kennedy Boulevard
Philadelphia, PA 19102-1679

Re: The School District of Philadelphia's Responses to City Controller's Report on Internal Control and on Compliance and Other Matters – Fiscal Year 2022

Dear Mr. Edacheril,

Please find the formal response from the School District of Philadelphia (SDP) to the findings identified in the Fiscal Year 2022 Report on Internal Control and on Compliance and Other Matters.

I would like to thank you and your staff for your efforts with respect to this audit.

Sincerely,

A handwritten signature in blue ink, appearing to read "Michael Herbstman".

Michael Herbstman
Chief Financial Officer

CC: William L. Streater, Esq., Board President, SDP Board of Education
Dr. Tony Watlington, Chief Executive Officer and Schools Superintendent
Lisa Huff, Audit Director, City Controller
Marcy Blender, Comptroller, School District of Philadelphia

2022-001 INADEQUATE REVIEW OF ACCESS CONTROLS AND SEGREGATION OF DUTIES RESPONSE

To address the audit finding of the security policy, The School District has taken the necessary steps to implement a formal plan. In order to do that with the components outlined in the finding, we have implemented a process for the security plan diagnosis which will lead to a formal policy to include: overall diagnosis, prescription and policy plan. This work began on 9/1/22 and is scheduled to conclude 3/31/23, as outlined in the below timeline. Most of the work has been completed as of the date of this response, 3/21/23.

1. Security Plan analysis 9/1/22 – 9/30/2022
 - Identify current roles and profiles of Finance positions - Complete
2. Duty Policy 10/1/22 – 1/31/23
 - Create a segmentation of duty policy where we have identified the incompatible roles – Complete
3. Security Plan Diagnosis 10/1/22 – 3/31/23
 - Identify risks in current security. All department reviews are complete. Of the 128 action items identified and documented, eight action items remain to be completed. The remaining eight action items will be completed by the end of March 2023
4. Annual Review
 - Perform annual review every May and complete each review at the end of the Fiscal Year.
5. Security Policy – 9/1/22 - 3/31/23
 - All steps above will be included in the overarching security policy for The School District. The policy was provided during the audit; however the policy will be updated to reflect the necessary changes including requiring an annual review.

2022-002 TERMINATION PAYMENTS REMAIN OUTSTANDING RESPONSE

The School District is pleased that the City Controller noted the substantial improvement in the continued focus on reducing the backlog of Termination Payments for the period through 2020. In comparison to last year's report, the number of term cases with term dates in fiscal year 2020 dropped from 402 to 28, with an outstanding dollar amount reduced from \$2.9 million to \$138 thousand.

The District has been able to both return to in-person processing and develop secure systems for remote processing. This will prevent future disruptions and allow for continued reduction of the current backlog. During a year of significant staff departures, Payroll staff continues to both pare down the backlog and keep pace with new separations aided by the Termination Pay application. As of mid-March 2023, all of the cases on the Vacation, Personnel, Illness, Leave (VPIL) report, which shows the termination pay outstanding, submitted for this audit have been processed. The majority of the term pay has not yet been finalized due to lack of Tax Sheltered Annuity ("TSA") paperwork. These will be submitted to VALIC, the TSA vendor for our orphaned account process. The remaining estate cases that have not submitted the requested paperwork will be paid to begin the escheatment process. The total existing backlog of cases for employees who separated in Fiscal Year 2022 number 172 (61 of which relate to employees over 55 who have not submitted TSA selections). The District expects to fully process all of these cases by the end of April 2023.

As recommended, the District will continue its unrelenting efforts to prioritize processing, with due diligence, for all outstanding termination payments owed to separated employees.

2022-003 INADEQUATE DEPROVISIONING OF SYSTEM ACCESS RESPONSE

This corrective action has now been completed. A programmatic solution was implemented in October 2022 that removes employee's role access when the employee is put into one of the statuses below in the Advantage HR system.. If the employee has role access to perform functions such as submitting requisitions, those roles are automatically removed as part of the programmatic solution for the following status codes:
O – Suspension; Z – No Pay; E – 89 Day Leave; T – Educational Leave; B – Sabbatical Leave

2022-004 NO FORMAL POLICY FOR CONFIGURATION CHANGES RESPONSE

The School District is currently implementing a formal process whereby all configurations will require a request and approval sign off. This work began in October 2022 and will conclude in March 2023.

1. Submitting process for configuration changes 10/1/22 – 3/31/23
 - The School District has developed Gravity forms, a plugin to our WordPress software which supports our Web publishing, as the mechanism to collect requests and approval for configuration changes. Testing is in progress and will be completed by the end of March 2023.
 - Currently, any configuration changes are being handled by email, with approval by the Department Head of the requester and is being tracked on a google spreadsheet. Because Oracle is cloud based, configuration changes are at a minimum. For example, for Fiscal Year 2022, there were only 13 configuration changes.
2. Configuration policy 1/31/23 – 3/31/23
 - A formal policy will be developed that describes requested changes relating to configuration to include itemizing the changes that need to be tracked and the process to request changes via Gravity forms.

2022-005 INADEQUATE MONITORING OF THIRD-PARTY SYSTEM CONTROL REPORTS RESPONSE

A standing quarterly meeting has been scheduled for the Information Technology Security team to review all relevant SOC-1 reports within 10 days of their release. The Quarter One 2023 meeting review was completed and the results can be found here:

Discussion:

- Reviewed both Oracle Fusion version 1 and 2 SOC-1 reports for the period of 1/1/2022-12/31/2022
- External auditor found that Oracle represented their definitions and controls accurately
- No exceptions noted and no areas of concern noted
- External auditor Ernst and Young found Oracle to be in compliance

Decisions Made:

- Since there were no exceptions or areas of concern, this SOC-1 report is deemed sufficient by the District